



Centrally Assessed and Industrial Properties

Revenue and Transportation Interim Committee

September 27, 2011

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Department of Revenue

REVENUE & TRANSPORTATION COMMITTEE
September 26 & 27, 2011 Meeting
September 27, Exhibit 20

Centrally Assessed and Industrial Property

- What is centrally assessed and industrial property?
- What are the numbers?
- What is the process and timelines for the appraisal and assessment of centrally assessed and industrial property?
- How is a centrally assessed property appraised?

What is Centrally Assessed Property?

Centrally assessed property is:

Properties Specifically Listed in 15-23-101, MCA and 42.22.102 (1), ARM

Railroad; railroad car; microwave; telecommunications; telephone cooperatives; gas utilities; electric utilities; electric cooperatives; ditch; canal; flume; natural gas pipeline; oil pipeline; and airlines.

AND

Physically Connected - Companies that actually have physically connected property that crosses a county or state boundary.

OR

Unity of Operation - Companies that have operating characteristics that exhibits unity where the property is functionally operated as a single entity but may not have a physical connection.

Central Assessment and Unit Valuation

- Unit valuation methodology is used to determine the market value of centrally assessed property
- Unit valuation involves “*appraising the whole pie and then taking Montana’s slice*”
 - appraising as a going concern, the entire operating property of a company – all of the company’s property located in the U.S.
 - allocating a part of that overall appraised value to Montana
- Unit valuation methods have been used to value centrally assessed property since the late 1800’s
 - Central assessment and unit valuation methods have been confirmed by the Montana Supreme Court in:
 - *Western Union Telegraph 1932, Yellowstone Pipe Line 1960, Puget Sound Power & Light Company 1988, PPL Montana 2007, PacifiCorp 2011, Puget Sound 2011*

What is Industrial Property?

- Industrial property is:

Property used in the extraction, production, distribution and changing the form of raw materials or assembling components and parts, packing and warehousing, and shipping of the finished products.

Includes all land, improvements to land, buildings, machinery and equipment

Examples of Industrial Property

Oil Refineries, Sawmills, Light Manufacturing, Grain Handling Facilities, Flour Mill, Coal and Metal Mines

What are the numbers?

	Property Class (Tax Rate)	2010 Number of Companies	2011 Number of Companies	2010 Market Value	2011 Market Value	Percent Change
Centrally Assessed Property:						
Railroad Companies	12 (3.45%)	9	9	\$1,351,514,889	\$1,900,696,369	40.6%
Utility and Electric Generation Companies	5 (3%), 9 (12%), 13 (6%), 14 (3%)	11	12	3,810,242,605	4,121,939,867	8.1%
Telecommunication Companies	13 (6%)	32	29	1,133,405,772	1,324,200,826	16.8%
Scheduled Airline Companies	12 (3.45%)	14	14	173,078,071	163,912,616	-5.3%
Telephone Cooperatives	5 (3%)	10	10	285,112,039	301,110,946	5.6%
Pipeline Companies	9 (12%)	21	22	950,078,760	1,174,647,127	23.6%
Electric Cooperatives	5 (3%)	35	35	642,391,640	675,884,345	5.2%
Total Centrally Assessed Property		132	131	\$8,345,823,776	\$9,662,392,096	15.8%
Industrial Property:						
Real Property	4 (2.72%)	-	-	\$942,385,555	\$980,224,702	4.0%
Pollution Control Property	5 (3%)	-	-	94,112,934	100,476,364	6.8%
Personal Property	8 (3%)	-	-	3,193,714,136	3,168,981,325	-0.5%
Electric Generation Property	13 (6%), 14 (3%)	=	=	230,519,476	214,767,338	-6.8%
Total Industrial Property		1,485	1,421	\$4,460,732,101	\$4,464,449,729	0.1%
Total Centrally Assessed and Industrial Property		1,617	1,552	\$12,806,555,877	\$14,126,841,825	10.3%
Total Statewide Market Value (2011 Market Value is estimated)				\$72,438,803,969	\$77,166,718,177	6.5%
Percent of Total Statewide Market Value				17.8%	18.3%	

September 27, 2011

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What is the Process and Timeline?

- All property is appraised as of January 1 (lien date)
- All property is appraised using the cost, income and market approaches when appropriate information is available
 - Railroads are valued using a statutory formula
- **Centrally Assessed Property:**
 - Appraised annually
 - All of the property owned by a centrally assessed companies; *e.g. buildings, land, equipment, and mileage property (think railroad track or power lines)*
 - No distinction is made between real or personal property in the appraisal process
- **Industrial Property:**
 - Real property is appraised on the same cycle as residential and commercial property; *e.g. buildings and land*
 - Personal property is appraised annually; *e.g. machinery and equipment*

The Process and Timeline

Centrally Assessed Property

- **Centrally Assessed Property Timeline:**
 - Companies report financial and operating information annually
 - Electric and Gas Utilities, Electric Generation, Telecommunication, Cooperatives annual reports are due *March 31* of each year
 - Railroads and Pipelines annual reports are due *April 15* of each year
 - Appraisals and informal reviews are conducted from *March 31* through *June 30* of each year
 - Values are certified with all other property; first Monday in *August*
- **Appeal Process:**
 - Business and Income Taxes Division (DOR) – Informal
 - Office of Dispute Resolution (DOR) – Formal
 - State Tax Appeal Board – Formal
 - District Court – Formal
 - Montana Supreme Court – Formal

The Process and Timeline

Industrial Property

- **Industrial Property Timeline:**
 - Real property is appraised cyclically (same cyclic as all class 4 property)
 - Established by the Legislature
 - Personal property is valued annually
 - Personal property reports are due 30 days after receipt of annual turnaround report
 - Appraisals and informal reviews are conducted from *March* through *July* of each year
 - Values are certified with all other property; first Monday in August
- **Appeal Process:**
 - Business and Income Taxes Division (DOR) – Informal
 - County Tax Appeal Board – Formal
 - State Tax Appeal Board – Formal
 - District Court – Formal
 - Montana Supreme Court – Formal

How is centrally assessed property appraised?

- The following slides provide a simple example of the appraisal and assessment process for a pipeline company.
- The example is of a fictitious company and situation.
- The example is meant to illustrate how the appraisal, allocation and apportionment of market value is determined.
- It is in no way meant to determine the true result of an appraisal, allocation, or apportionment for any actual company or any actual situations.

Centrally Assessed/Unit Valuation Definitions

System or unit market value – the market value of all assets owned by the company being appraised

Allocation – process of assigning the system or unit market value to Montana

Montana market value – the market value of all the Montana property

Apportionment – the process of assigning the Montana market value to the proper taxing jurisdiction

Situs property – real and personal property (machinery, equipment, buildings and land)

Mileage property – railroad track, power lines, telecommunication underground cable or pipelines

Western Pipeline Company

Unit Valuation

Three Approaches to Determine Market Value:

Cost Approach:

- Original or historic cost less depreciation
- Information comes from the balance sheet and other audited records

Income Approach:

- Discounting an income stream
- Information comes from income statements and financial markets

Market Approach:

- Market value of the equity and debt
- Comparable sales of like property
- Information comes directly from the market

Western Pipeline Company

Company Facts:

- Owns gathering and transmission assets in 10 western states
- Files the following reports with the Department of Revenue:
 - DOR Montana Annual Report
 - FERC Report
 - SEC 10-K
 - Independent Auditor's Reports
- Appraisal is for tax year 2011 (lien date January 1, 2011)

Western Pipeline Company

Cost Approach

Original Cost Less Depreciation:

Plant in service	\$ 750,000,000
Materials and supplies	\$ 1,000,000
Construction work in progress	\$ 5,000,000
Less accrued depreciation	<u>\$(104,000,000)</u>
Cost indicator before intangible personal property	\$ 652,000,000
Less intangible personal property (5% reduction)	<u>\$ (32,600,000)</u>
Cost indicator after intangible personal property	\$ 619,400,000

Western Pipeline Company

Income Approach

Capitalization of Income:

Net operating income:

Year-end 2008	\$ 57,000,000	
Year-end 2007	\$ 60,000,000	
— Average net operating income		\$ 58,500,000
Capitalization rate		<u>÷ 9%</u>

Income indicator before intangible personal property	\$650,000,000
Less intangible personal property (5% reduction)	<u>\$(32,500,000)</u>

Income indicator after intangible personal property	\$617,500,000
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Western Pipeline Company

Market Approach

Stock and Debt:

Stock (equity):

Shares outstanding	30,000,000
Average price per share	<u>x \$ 17.00</u>
– Market value of common stock	

\$510,000,000

Debt (bonds):

Long term debt

\$135,000,000

Market indicator before intangible personal property

\$645,000,000

Less intangible personal property (5% reduction)

\$(32,250,000)

Market indicator after intangible personal property

\$612,750,000

Western Pipeline Company

System Market Value

Cost approach *page 14*

\$ 619,400,000

Income approach *page 15*

\$ 617,500,000

Market approach *page 16*

\$ 612,750,000

System Market Value

\$ 615,000,000

Western Pipeline Company Allocation Factor

Montana / All States = Factor

Book (gross) cost \$120,000,000 / \$756,000,000 = 0.16 or 16%

Gross revenues \$25,000,000 / \$119,500,000 = 0.21 or 21%

Miles of pipe 4,175 miles / 17,500 miles = 0.24 or 24%

Average Montana allocation factor $\{((.16 + .21 + .24)/3) = .20\}$ = 0.20 or 20%

Western Pipeline Company

Montana Market Value

System Market Value *page 17*

\$ 615,000,000

Montana Allocation Factor *page 18*

x 20%

Montana Market Value

\$ 123,000,000

Western Pipeline Company

Apportionment to County/Levy Districts

- Market Value (MV) of an individual asset is determined by apportioning the Montana Market Value to the individual asset(s)
- Assets Book Cost x Market to Book Ratio = Asset MV
- Western Pipeline Co. operates in 3 Montana Counties; Powell, Silver Bow, and Deer Lodge
 - Assets Book Cost by County:
 - Powell \$90,000,000
 - Silver Bow \$25,000,000
 - Deer Lodge \$5,000,000
 - TOTAL page 18 \$120,000,000

Western Pipeline Company

Apportionment to County/Levy District – Cont.

- Market Value/Book Cost = Market to Book Ratio (M/B)
- Montana Market Value = \$123,000,000 *page 19*
- Total Assets Book Cost = \$120,000,000 *page 18*
- $\$123,000,000 / \$120,000,000 = 1.025 \text{ M/B}$

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Apportionment to County/Levy District – Cont.

	Original Cost	x M/B =	Asset MV
• Powell	\$ 90,000,000	x 1.025 =	\$92,250,000
• Silver Bow	\$ 25,000,000	x 1.025 =	\$25,625,000
• Deer Lodge	<u>\$ 5,000,000</u>	x 1.025 =	<u>\$5,125,000</u>
• TOTAL	\$120,000,000		\$123,000,000

Assume 3 levy districts in Deer Lodge County

• District City	\$1,000,000	x 1.025 =	\$1,025,000
• District Rural	\$3,000,000	x 1.025 =	\$3,075,000
• District Spec	<u>\$1,000,000</u>	x 1.025 =	<u>\$1,025,000</u>
• TOTAL	\$5,000,000		\$5,125,000

Western Pipeline Company

Tax Calculation for Deer Lodge County

	Asset MV	x	TR	x	Mill	=	Tax
District City	\$1,025,000	x	.12	x	.500	=	\$61,500
District Rural	\$3,075,000	x	.12	x	.500	=	\$184,500
District Spec	<u>\$1,025,000</u>	x	.12	x	.500	=	<u>\$61,500</u>
TOTAL	\$5,125,000						\$307,500

Asset MV = Market Values from page 22

TR = Tax Rate 12%

Mill = Mill Levy 500

